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The Manufacturers Hanover
Financial Digest
Economic Commentary, Selected Financial Data, and Business Indicators

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Declining Energy Prices . . .

After five years of battling the worst economic crisis since the days of the Great Depression, American farmers are beginning to see scattered signs suggesting that the agricultural economy may be nearing the bottom of its slide. At long last, some relief from the deteriorating financial conditions that have battered so much of the U.S. agricultural sector seems to be in the offing. Lower oil prices and interest rates as well as declining fertilizer and land rental costs have reduced farm expenses and brightened profit potentials for financially healthy farmers.

The most important factor in the brighter outlook for American agriculture is the decline in farmers' costs of operation. Farmers' cash expenses dropped by an estimated $5 billion in 1985 and are expected to fall an additional $5 billion to $6 billion this year—the first time since the early 1930s that farmers' cash expenses have declined for two consecutive years.

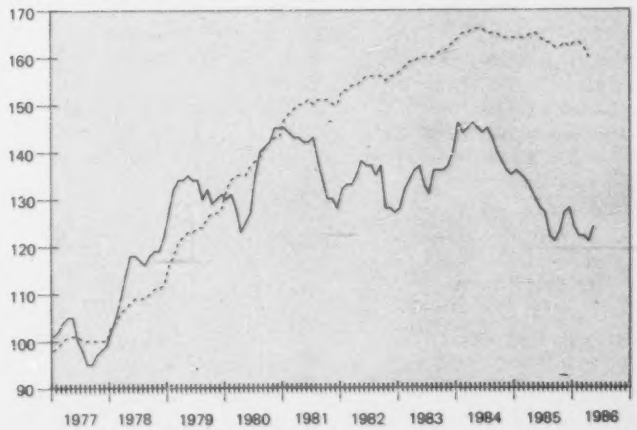
The drop in farmers' operating costs comes from three main sources: Lower energy prices and a related drop in such petroleum-based inputs as fertilizers, lower interest expenses resulting from lower interest rates and declining farm debt, and finally, a reduction in planted acreage due to wide participation of farmers in government programs with substantial set-aside requirements.

Lower fuel costs will have the largest impact on the reduction of farmers' expenses. From 1973 to 1981, energy costs as a percentage of total production outlays increased continuously, reaching a high of 6.3 percent in 1981. However, this year farmers' fuel bills may account for only four percent of their total expenses—the lowest share since 1974. In addition, the decline in fuel prices will also have broad secondary effects, cutting prices for related items such as fertilizers and pesticides.

. . . And Lower Interest Rates . . .

Interest expenses are also expected to decline significantly in 1986. These payments as a percentage of total production expenses more than doubled between 1970 and 1982. Since 1982, they have declined slightly, but a sharper drop is expected to take place this year. Total farm debt outstanding will likely register a small decline in 1986—the third drop in a row. Real estate debt should fall as farmers pay off old debts rather than acquire new land, while non-real estate debt will decline because the reductions in acres planted, input prices and capital expenditures lessen the need of external capital for many farmers.

INDEX OF PRICES RECEIVED BY FARMERS (LINE) VS. INDEX OF PRICES PAID BY FARMERS (DOT) <1977=100>



Source: U.S. Department of Agriculture

Finally, farmers have already placed 3.8 million acres of their more erodible farmland into a long-term conservation reserve. Under a new five-year farm bill enacted last December, the U.S. Department of Agriculture will pay farmers to plant trees or grass on that land. The bill's goal is for farmers ultimately to place 40 million to 45 million acres, about ten percent of the nation's total farmland, in reserve by the end of 1990. Since farmers will plant fewer acres, they will need a smaller quantity of production inputs, thus spending fewer dollars to grow their 1986 crops. On the other hand, idle acreage will mean lost sales for chemical, seed, equipment, transportation and other businesses that supply farmers.

. . . Spell Some Relief For American Farmers

In addition to lower costs of production inputs, farm income will also be boosted by government

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farm program payments which could total a record $10 billion to $13 billion for 1986. Government payments could add up to nine percent of farmers' gross income this year, compared with approximately 4½ percent in 1985.

Notwithstanding these positive factors, net cash income, however, may not rise this year. This is because farmers' expenses are not falling in step with the prices they receive for their output. During the 12 months ending in April, farmers' costs of operation declined only 2½ percent, while farmgate prices dropped over eight percent, reaching one of the lowest levels since the end of 1978 (see chart on page 1). Bumper harvests of the past few years produced an oversupply of farm commodities, depressing their prices. Although fewer acres were planted this year, better-than-normal weather conditions are expected to produce another good harvest, pushing already bin-busting surpluses of farm commodities higher and prices lower.

As a result, farmers' crop receipts are expected to fall this year. This, of-course, will cut into farmers' gross income. Thus, lower farm costs and higher government payments will be offset by declining receipts for farmers' output. Not surprisingly, the U.S. Department of Agriculture now projects that farmers' net cash income in 1986 will just about

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/18/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	192.318	+ 2.370	+17.963
Loans to Depository Inst.	.734	+ .031	− .693
Float	1.067	+ .348	+ .269
Total Reserve Bank Credit	209.437	+ 3.091	+20.947
Treasury Deposits with Federal Reserve Banks	3.075	+ .600	+ .561
Currency in Circulation	198.880	+ .234	+13.240
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	148.407	+ 1.417	+26.006
	6/18/86		
Member Bank Reserves:			
Total Reserves Held	49.495	+ 1.635	+ 6.786
Excess (Deficiency)	.707	− .292	− .017
Net Free Reserves	.514	− .180	+ .301

Monetary Aggregates †		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (6/9/86)	666.9	+ 18.1‡	+ 13.1‡
M2 (May '86)	2,647.0	+ 10.9	+ 8.0
M3 (May '86)	3,306.6	+ 8.3	+ 7.7
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 6/20/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.26%	6.47%	6.60%
* Federal Agencies	6.49	6.63	6.76
* Municipal Notes—High Grade (46% Taxable Equivalent)	6.48	6.94	8.15
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.67	6.65	7.00

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.70%	Jul.	6.80%
15- 29 days	6.70	Aug.	6.75
30- 59 days	6.60	Sep.	6.65
60- 89 days	6.45	Oct.	6.60
90-179 days	6.25	Nov.	6.50
180-239 days	6.12	Dec.	6.45
240-270 days	6.12		

‡ Industrial Paper—Prime			
30- 89 days	6.67%	†Federal Funds Effective Rate	6.80%
90-120 days	6.61		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'86	$ 4,116r	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q'86	$ 3,617r	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q'86	2.9r	0.7	3.7
Change in Consumer Prices*	May '86n	2.4%	− 3.6%	2.4%
Change in Producer Prices*	May '86n	7.2%	− 7.2%	2.4%
Civilian Employment (Thousands of Persons) †	May '86	109,110	108,892	106,939
Unemployment as % of Civilian Labor Force†	May '86	7.3%	7.1%	7.3%
Personal Income*	May '86n	$ 3,445	$ 3,448r	$ 3,271
Leading Indicators Composite Index (1967=100)†	Apr '86	179.2	176.6	166.7
Industrial Production Index (1977=100) †	May '86n	124.2	125.0r	124.1
Net Change in Consumer Installment Credit †	Apr '86	$ 4.16	$ 3.09	$ 7.54
U.S. Merchandise Trade Balance †	Apr '86	−$ 12.07	−$ 12.18	−$ 12.11
Plant and Equipment Expenditures*	3rd Q'86n	$388.87(a)	$387.42(a)r	$388.90
Private Housing Starts (Thousands of Units)*	May '86n	1,888	2,039r	1,684
New Construction Expenditures*	Apr '86	$ 356.7	$ 353.9	$ 341.9
Total Business Inventories †	Apr '86n	$ 590.2	$ 588.2r	$ 578.5
Total Business Sales †	Apr '86n	$ 426.3	$ 420.2r	$ 423.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

match last year's levels—somewhere between $42 billion and $46 billion.

But while farmers will have more cash in their pockets, the overall financial picture of the farm sector could worsen slightly this year as deflation in farmland prices continues to erode the value of farmers' assets and net worth. The value of farmland, which accounts for the bulk of the total value of all farm assets, declined 12 percent in 1985, matching the previous year's fall—the largest since the Great Depression. This tumble marked the fifth consecutive year of falling prices for farmland. This year, however, the decline should be much smaller. Surveys in many parts of the nation's farm belt indicate that the decline in land values slowed in the first quarter, and many respondents felt that land values would stabilize in the second quarter.

To be sure, any recovery in the farm sector from the devastating slump of the recent years will be slow and uneven. It may not arrive soon enough for some of the farmers facing severe financial stress, asset liquidations, problems in obtaining credit and even bankruptcy. But the adjustments and changes in the farm sector, while hard and painful, are improving the financial conditions of farmers and slowly setting a stage for an improvement in the nation's important agricultural sector. H

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (6/4/86)	155,476	+ 44	– 62
New York City (6/11/86)	34,428	– 347	+ 1,418
Commercial Paper (6/11/86)	312,002	+ 195	+51,930

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/4/86)	259,627	+ 1,555	+ 4,099
New York City (6/11/86)	56,603	– 139	– 4,674

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/4/86)	738,080	+ 4,180	+ 57,309
New York City (6/11/86)	159,971	– 608	+ 8,853

Financial Markets

	Friday 6/20/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.25%	– .09	– .97
180-Day Bills†	6.43	– .09	– 1.14
Longest Bills†	6.57	– .07	– 1.33
Recent Issues:			
7s 6/30/88 (When Issued)	7.09	NA	
7 1/4s 3/31/90	7.40	– .12	
7 3/8s 5/15/96	7.60	– .14	
7 1/4s 5/15/16	7.45	– .09	
Municipals:			
Bond Buyer–20 Bond Index* (6/19/86)	7.82%	– .20	– .87
Blue List Total ($ Million)	$1,850	–$ 247	– $ 244
30-Day Visible Supply ($ Million)	$3,060	–$1,410	+ $ 388
Total	$4,910	–$1,657	+ $ 144
Corporates:			
Moody's Aa Composite (6/19/86)	9.48%	– .12	– 1.87
30-Day Visible Supply ($ Million)	$3,845	+$ 25	+ $2,492
Stocks:			
Dow-Jones Averages:			
Industrials	1,879.54	+ 5.35	+ 555.39
Transportation	778.13	– 8.37	+ 128.55
Utilities	190.49	+ 2.80	+ 23.64
65 Stocks	717.61	+ .55	+ 171.17
N.Y.S.E. Composite Index	141.65	+ .65	+ 31.80
N.Y.S.E. Avg. Daily Vol. for Week (000's)	126,200	+ 888	+ 24,132

* 46% Taxable equivalent 14.48%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 6/20/86	Week Ago
Overnight	6.81%	6.81%
1 month	6.94	6.94
3 month	6.88	6.94
6 month	6.88	6.94
1 year	7.06	7.12
EURODOLLAR BONDS Average Yield		
Medium Term (5 to 7 yrs.)	7.30%	8.04%
Long Term (7 to 15 yrs.)	7.77	8.19

FOREIGN EXCHANGE SPOT RATES

New York Opening (6/20/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02181	45.85
Canada	.7198	1.3893
Denmark	.1200	8.3300
France	.1397	7.1575
Germany	.4458	2.2430
Italy	.0006496	1539.50
Japan	.005968	167.55
Mexico	.001617	618.50
Netherlands	.3960	2.5255
Switzerland	.5419	1.8453
U.K.	1.5015	.6660

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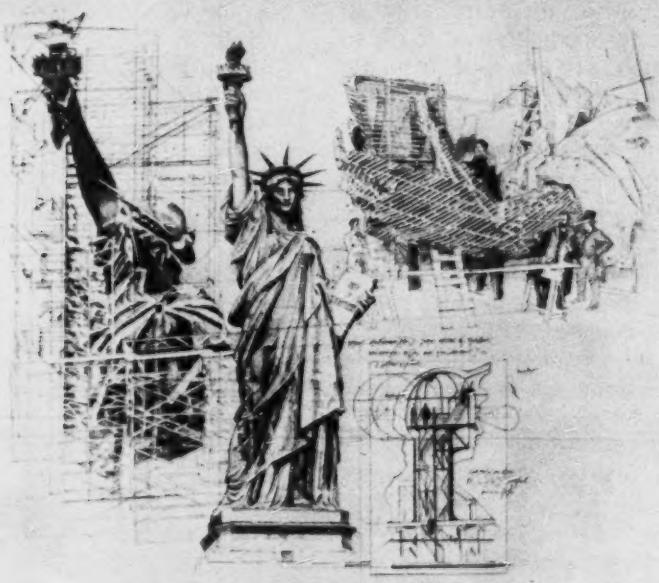

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